No. 11,556

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

MAGNESIUM PRODUCTS, INC., a corporation,

Appellant,

vs.

NORTH AMERICAN AVIATION, INC., a corporation, and UNITED STATES OF AMERICA,

Appellees.

BRIEF OF APPELLEES.

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TABLE OF AUTHORITIES CITED

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BRIEF OF APPELLEES.

Jurisdictional Statement.

Appellant filed its complaint in the District Court alleging that it is a California corporation; that appellee, North American Aviation, Inc., is a Delaware corporation; and that the matter in controversy exceeds, exclusive of interest and costs, the sum of $3000. The amount sued for is $20,204.03.

Jurisdiction of the District Court is established by 28 U. S. C. 41. Jurisdiction of this court is established by 28 U. S. C. 225.

Statement of the Case.

The complaint sets forth two causes of action. The first cause of action is the common count for the agreed price of goods sold and delivered by plaintiff to defendant at its request. The second cause is the common count on an account stated.

The answer admits that defendant became indebted to plaintiff in the sum of $20,204.03; that no part of said sum has been paid to the plaintiff; that demand has been made therefor; that defendant refuses to pay said sum or any part thereof to plaintiff because renegotiation had taken place between the Under-Secretary of War and the plaintiff pursuant to the provisions of the Renegotiation Act, for the purpose of eliminating excessive profits realized by the plaintiff during its fiscal year ended November 30, 1942, under its contracts and sub-contracts subject to renegotiation; that the Under-Secretary of War, on or about June 6, 1944, found and determined that $250,000 of the profits realized by plaintiff during its said fiscal year, under its contracts and sub-contracts subject to renegotiation, were excessive; and that thereafter the Under-Secretary of War caused to be served on defendant a series of withholding orders requiring defendant to withhold for the account of the United States from moneys otherwise due or which thereafter became due from the defendant to the plaintiff, the sum of $20,204.03, which sum plaintiff has withheld and still withholds, pursuant to said orders, and which said sum is the amount claimed by the plaintiff. [R. 2-25.]

Upon motion of the United States, pursuant to the provisions of the Act of August 24, 1937, 28 U. S. C. 401, and the provisions of Rule 24 of the Federal Rules of Civil Procedure, an order was entered permitting the United States to intervene. Thereupon the United States filed its answer setting forth seven defenses. [R. 48-60.]

The second defense set forth in the answer of the United States avers that the court has no jurisdiction of any issue as to which the Tax Court is given jurisdiction by Section 403(e) of the Renegotiation Act; that plaintiffs have filed a petition in the Tax Court for a redetermination but that the Tax Court has not as yet heard or decided plaintiff's case; and that this suit is premature because plaintiff has not as yet exhausted its Tax Court remedy. [R. 55.]

The fourth defense set forth in the answer of the United States avers the renegotiation and withholding orders substantially as set forth in the answer of the defendant and in addition thereto, avers that plaintiff has filed a petition in the Tax Court of the United States asking for a redetermination of the amount, if any, of its excessive profits for its fiscal year ending November 30, 1942, and that the Tax Court has not as yet heard plaintiff's case or rendered its decision thereon. [R. 56.]

At the trial the facts were stipulated as follows:

After due notice to the plaintiff, proceedings for the renegotiation of plaintiff's contracts and sub-contracts were had by representatives of the Secretary of War and

thereafter, on the sixth day of June, 1944, the Under-Secretary of War, acting under and by virtue of the Renegotiation Act and pursuant to authority delegated to him, duly determined in accordance with law that of the profits realized by plaintiff during the fiscal year ending November 30, 1942, on those contracts and sub-contracts subject to renegotiation, $250,000 thereof were excessive profits; that the document annexed to the answer of intervenor United States of America as Exhibit A is a carbon copy of the order of determination made and signed by the Under-Secretary of War on the 6th day of June, 1944; that the tax credit to which plaintiff is entitled under Section 3806 of the Internal Revenue Code is $184,376.63; that pursuant to the Renegotiation Act the Under-Secretary of War mailed to the defendant North American Aviation, Inc., a directive to withhold moneys from Magnesium Products, Inc., pursuant to the Renegotiation Act, which order was amended by subsequent telegrams and letters; that pursuant to these directives from the Under-Secretary of War the defendant has withheld for the use and account of the United States from amounts otherwise due to plaintiff, the sum of $20,204.03; that plaintiff has filed a petition in the Tax Court of the United States asking for a determination of the amount, if any, of its excessive profits for its fiscal year ended November 30, 1942; that the Tax Court has not as yet heard plaintiff's case or rendered any decision thereon; that said amount of $20,204.03 now being withheld by defendant from plaintiff, pursuant to the

withholding orders aforesaid, represents amounts accrued to the credit of plaintiff as the result of its performance of the work provided for by purchase orders, all of which required the furnishing of materials and parts for the construction of airplanes for use by the United States in the promotion of the war effort; and that the amount now due the United States on account of the renegotiation indebtedness referred to in this stipulation, is at least equal to, or more than, the amount of $20,204.03 now being withheld by defendant.

It was further stipulated:

"Mr. Bailey: On that statement of facts, Your Honor, we will so stipulate. Now, in addition to that there has been filed on the various motions for summary judgment, an affidavit of E. R. Clayton on behalf of plaintiff, and there has been filed an affidavit of Robert P. Patterson, and an affidavit of H. Sturde Hensel on behalf of the United States.

We will stipulate that if these witnesses were called, that they would testify substantially as they have in these affidavits.

Mr. Wright: And that is with the understanding, of course, that none of the facts set forth in any of the affidavits shall result in any way qualifying the stipulation as to the facts relating to the issues raised by the pleadings, which issues are now on trial.

Mr. Bailey: Yes, it is so understood and stipulated." [R. 248-251.]

SUMMARY OF ARGUMENT.

I.

The Tax Court Has Exclusive Jurisdiction to Decide All Questions Presented by Appellant, Except the Question of the Power of Congress to Enact the Statute.

(a) The administrative procedure provided by the Renegotiation Act is constitutional.

(b) The rule requiring exhaustion of an administrative remedy is one of judicial administration—not merely a rule governing the exercise of discretion—and is applicable to proceedings at law as well as suits in equity.

II.

The Renegotiation Act Is Not Subject to the Constitutional Objections Advanced by Appellant.

ARGUMENT.

I.

The Tax Court Has Exclusive Jurisdiction to Decide All Questions Presented by Appellant Except the Question of the Power of Congress to Enact the Statute.

Section 403(e)(1) of the Renegotiation Act (Public Law 235, 78th Congress, 2nd Sess.) provides:

> "Any contractor or subcontractor aggrieved by an order of the Board determining the amount of excessive profits received or accrued by such contractor or subcontractor may, within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the last day), after the mailing of the notice of such order under subsection (c)(1), file a petition with The Tax Court of the United States for a redetermination thereof. Upon such filing such court shall have *exclusive jurisdiction,* by order, to finally determine the amount, if any, of such excessive profits received or accrued by the contractor or subcontractor, and such determination shall not be reviewed or redetermined by any court or agency. The court may determine as the amount of excessive profits an amount either less than, equal to, or greater than that determined by the Board. A proceeding before the Tax Court to finally determine the amount, if any, of excessive profits shall not be treated as a proceeding to review the determination of the Board, but shall be treated as a proceeding *de novo.* For the purposes of this subsection the court shall have the same powers and duties, insofar as applicable, in respect of the contractor, the subcontractor, the Board and the Secretary, and in respect of the attendance of witnesses and the production of papers, notice of

> hearings, hearings before divisions, review by the Tax Court of decisions of divisions, stenographic reporting, and reports of proceedings, as such court has under sections 1110, 1111, 1113, 1114, 1115(a), 1116, 1117(a), 1118, 1120, and 1121 of the Internal Revenue Code in the case of a proceeding to redetermine a deficiency. In the case of any witness for the Board or Secretary, the fees and mileage, and the expenses of taking any deposition shall be paid out of appropriations of the Board or Department available for that purpose, and in the case of any other witnesses, shall be paid, subject to rules prescribed by the court, by the party at whose instance the witness appears or the deposition is taken. The filing of a petition under this subsection shall not operate to stay the execution of the order of the Board under subsection (c)(2)." (Italics added.)

Appellant, whose fiscal year ended prior to July 1, 1943, is accorded the same remedy by Section 403(e)(2) of the Act.

In *Myers v. Bethlehem Corp.*, 303 U. S. 41, it was contended that rights guaranteed by the Constitution would be denied unless it be held that the District Court has jurisdiction to enjoin the holding of a hearing by the Labor Relations Board. At page 50 the Court said:

> "So to hold would, as the Government insists, in effect substitute the District Court for the Board as the tribunal, to hear and determine what Congress declared the Board exclusively should hear and determine in the first instance. The contention is at war with the long settled rule of judicial administration that no one is entitled to judicial relief for a supposed or threatened injury until the prescribed

> administrative remedy has been exhausted. That rule has been repeatedly acted on in cases where, as here, the contention is made that the administrative body lacked power over the subject matter."

At about the time appellant's brief was filed in this case, the Supreme Court, on June 16, 1947, filed its opinion in the case of *Aircraft & Diesel Equipment Corp. v. Hirsch,* No. 95, October Term 1946. In that case, Aircraft, while its petition for a redetermination of its excessive profits was pending and undisposed of in the Tax Court, sought a declaratory judgment, of the District Court, that the First and Second Renegotiation Acts are unconstitutional, and an injunction restraining defendants from taking steps (issuing withholding orders) to prevent payment of moneys owed to it by its customers-prime contractors. In that case the Supreme Court held that the doctrine of exhaustion of administrative remedies applies to such issues as statutory coverage and amount, and that on those issues the subcontractor could have no relief, either in equity or in a suit against the prime contractor, until, at least, after termination of the Tax Court proceedings.

The contentions made at pages 36 and 37 of appellant's brief: (a) that the Secretary has renegotiated purchase orders which were not sub-contracts, and (b) that the Secretary has renegotiated contracts in sums less than $100,000, present questions of coverage—not open for decision by the District Court in this case. This Court so held in the *Pownall* case (159 F. (2d) 73).

(a) Administrative Procedure Provided by the Renegotiation Act Is Constitutional.

It will be noted that Section 403(e) provides that the Tax Court, in considering cases presented to it under the Renegotiation Act, is controlled by the statutory provisions that control it in the case of a proceeding to redetermine a deficiency. An examination of the sections of the Internal Revenue Code referred to in Section 403(e) of the Act demonstrates that the authorized procedure provides for a full and fair hearing and determination of all matters of fact and that, through judicial review, it provides for the protection of all the legal rights of the petitioner, including any constitutional right which it may be entitled to invoke. While Section 403(e) of the Act does not specifically provide for judicial review of the Tax Court's determinations of questions of law, it seems clear, nevertheless, that it was not the intent of the Congress to abolish the jurisdiction of the Circuit Courts of Appeals (26 U. S. C. 1141) to review decisions of the Tax Court in cases brought pursuant to the Renegotiation Act. This proposition is demonstrated with convincing logic by the Court of Appeals of the District of Columbia in the case of *U. S. Electrical Motors, Inc., v. Jones,* 153 F. (2d) 134. This conclusion is also sustained by the reasoning in the case of *Anniston Manufacturing Co. v. Davis,* 301 U. S. 337.

(b) The Rule Requiring Exhaustion of an Administrative Remedy Is One of Judicial Administration—Not Merely a Rule Governing the Exercise of Discretion—and Is Applicable to Proceedings at Law as Well as Suits of Equity.

The language of the caption is the language of the Supreme Court in its opinion in the case of *Myers v. Bethlehem Corp.*, 303 U. S. 41, set forth in note 9 at page 51 of the opinion. The court cites *First National Bank v. Board of County Commissioners*, 264 U. S. 450, 455, and *Anniston Manufacturing Co. v. Davis*, 301 U. S. 337, 343—both suits at law. It is submitted that these two cases sustain the proposition in support of which they are cited, and their logic sustains the Government's contention that the Tax Court has exclusive jurisdiction to decide, in the first instance, all questions presented by appellant, except the basic constitutional question of the power of Congress to enact the statute.

II.

The Renegotiation Act Is Not Subject to the Constitutional Objections Advanced by Appellant.

The Supreme Court decided, in *Aircraft & Diesel Corp. v. Hirsch,* that the subcontractor in that case had an adequate remedy at law by suit upon its contracts against its customers (prime contractors), and that in such suit the question of the constitutional power of Congress to enact the Act could be presented and determined.

In *Spaulding et al. v. Douglas Aircraft Co.,* 154 F. (2d) 419, this Court passed upon each of the constitutional questions presented by appellant and decided each contrary to appellant's contention. In *U. S. v. Pownall et al.,* 159 F. (2d) 73, this Court, upon a re-examination of the constitutional questions presented, adhered to its decision in the *Spaulding* case.

For the reasons above set forth, it is respectfully submitted that the judgment of the District Court should be affirmed.

Respectfully submitted,

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